BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
)
R. G. AND MARTHA G. HOLLIDAY)

For Appellants: Martha G. Holliday, in pro. per.

For Respondent: Lazaro L. Bobiles Counsel

O P I N I O N

This appeal is made pursuant to section 18593, of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of R. G. and Martha G. Holliday against a proposed assessment of additional personal income tax in the amount of $214 for the year 1980.

The issue presented is whether appellant-husband is entitled to deduct from gross income an individual retirement account contribution for 1980.

Appellants filed a joint California personal income tax return for 1980, claiming a deduction of a contribution each made to an individual retirement account (IRA). Respondent determined that neither appellant was entitled to make a deductible IRA contribution for 1980 and disallowed both deductions. It also disallowed a medical expense deduction claimed by appellants. Respondent issued a proposed assessment which was affirmed after appellants' protest. This timely appeal followed. Respondent concedes that deduction of Mrs. Holliday's IRA contribution and the medical expense should have been allowed. The sole issue remaining is whether Mr. Holliday's IRA contribution was deductible. Hereafter, "appellant" shall refer to Mr. Holliday.

Appellant was employed by Industrial Indemnity for a period of three years ending in September 1980. Industrial Indemnity maintained a pension plan which was qualified under section 17501 of the Revenue and Taxation Code and which included a trust exempt from tax under section 17631 of the Revenue and Taxation Code. Appellant's pension benefits under the qualified plan were not vested and were forfeited by appellant when his employment with Industrial Indemnity ended. 'During the remainder of 1980, appellant was not a participant in his subsequent employer's qualified plan. Appellant established an IRA and contributed $1,500 to it for 1980.

Section 17240 of the Revenue and Taxation Code allows a deduction for cash contributions to an IRA. No deduction is allowable, however, to an individual who, at any time during the taxable year, was an "active participant" in an employer pension, profit-sharing, or stock bonus plan which is described in section 17501 and includes a trust exempt from tax under section 17631. (Rev. & Tax. Code, § 17240, subd. (b)(2)(A)(i).)

Respondent contends that it properly disallowed the claimed deduction because appellant was an active participant in his employer's qualified pension plan. Appellant argues that he should be allowed the deduction because he forfeited his-benefits under the plan.

Essentially the same situation has been before this board in several appeals. (Appeal of Neil1 0. and Alice M. Rowe, Cal. St. Bd. of Equal., Aug. 17, 1982;

Appeal of Gerald G. Marans, Cal. St. Bd. of Equal., Dec. 10, 1981.) In those appeals, we held that the taxpayer was an active participant in his employer's pension plan even though he received no benefits and, in fact, forfeited all accrued benefits when his employment ended. We explained that the taxpayer is an active participant in his employer's plan if benefits under that plan were, accrued on behalf of the taxpayer during any part of the taxable year, even if he later forfeited those benefits.

Appellant argues that a taxpayer should be allowed to deduct an IRA contribution in a taxable year even though he accrued benefits under a qualified plan during that year as long as he forfeited those benefits and had no chance of having them reinstated. The position taken by appellant was accepted by the Seventh Circuit Court of Appeals in Foulkes v. Commissioner, 638 F.2d 1105 (7th Cir. 1981), but rejected by the Third Circuit in Hildebrand v. Commissioner, 683 F.2d 57 (3d Cir. 1982). We need not decide whether we agree with the Foulkes rationale since that case is distinguishable from the appeal before us. The Foulkes decision was grounded on the fact that there was no possibility that the benefits forfeited by the taxpayer could be reinstated to him. This is not true in the case before us.

Industrial Indemnity's pension plan contains a break-in-service provision under which appellant would be entitled to reinstatement of his forfeited benefits if he was re-employed by Industrial Indemnity within a certain amount of time. Appellant argues that we should disregard that provision because the circumstances surrounding his departure from Industrial Indemnity made it unlikely that he would be re-employed. We cannot agree. Although it was not highly probable that appellant would be re-employed by Industrial Indemnity, it remained possible; it therefore remained possible for him to have his benefits reinstated. Such potential distinguishes this appeal from Foulkes v. Commissioner, supra.

For the above reasons, we conclude that respondent properly disallowed appellant's claimed IRA deduction. The action of respondent, as revised in accordance with its concessions, must therefore be sustained.

Appeal of R. G. and Martha G. Holliday

O R D E R

Pursuant to the views expressed in the opinion of the board on file -in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to section 18595 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protest of R. G. and Martha G. Holliday against a proposed assessment of additional personal'income tax in the amount of $214 for the year 1980, be and the same is hereby modified in accordance with respondent's concessions. In all other respects, the action of the Franchise Tax Board is hereby sustained.

Done at Sacramento, California, this 17th day Of January, 1984, by the State Board of Equalization, with Board Members Mr. Nevins, Mr. Dronenburg and Mr. Bennett present.

Richard Nevins, Chairman

Ernest J. Dronenburg, Jr., Member

William M. Bennett, Member

_____, Member

_____, Member